State of California
Franchise Tax Board

2007 Guidelines for Corporations Filing A Combined Report

See Cal. Code Regs., tit. 18 section 25106.5 through 25106.5-11 for combined reporting definitions and procedures adopted under Section 25106.5 of the Revenue and Taxation Code.

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- Form 100, California Corporation Tax Booklet
- Form 100W, Water's-Edge Booklet
- FTB Pub. 1038, Guide to Dissolve, Surrender, or Cancel a California Business Entity
- FTB Pub. 1050, Application and Interpretation of Public Law 86-272
- FTB Pub. 1060, Guide for Corporations Starting Business in California
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Corporations Filing a Combined Report

Introduction

This publication sets forth the concepts of the unitary method of taxation and its application by the State of California to corporations subject to either the franchise tax or income tax. It includes instructions for preparing a combined report, which a corporation is required to use in computing its California tax liability, when the corporate activities are part of a unitary business conducted by the corporation and its related corporations. A combined report is not equivalent to a consolidated return for federal purposes.

This publication does not address water's-edge statutes under which corporate taxpayers may elect to exclude from the combined report some or all of the income and apportionment factors of certain foreign affiliates in the unitary group. For more information about the water's-edge election, get Form 100W, Water's-Edge Booklet.

Important Information

Regulations providing detailed rules regarding the general mechanics of combined reporting are in Cal. Code Regs., tit. 18 section 25106.5 through 25106.5-11. Because those regulations reflect long-standing practices of the Franchise Tax Board, the regulations generally apply retroactively. In addition, those rules adopt, for accounting periods beginning on or after April 22, 1999, apportionment rules substantially reflecting the holdings of the Board of Equalization in *Appeal of Huffy, Corp.,* 99-SBE-005, April 22, 1999, and *Appeal of Joyce, Inc.*, 66-SBE-069, November 23, 1966, and FTB Legal Ruling 234.

Regulations providing detailed rules relating to the treatment of intercompany transactions between members of a combined reporting group were adopted (Cal. Code Regs., tit. 18 section 25106.5-1). Those regulations apply to intercompany transactions that occur between members in taxable years beginning on or after January 1, 2001.

In *Farmer Bros. Co. v. Franchise Tax Board* (2003) 108 Cal App 4th, 134 Cal Rptr. 2nd 390, the California Court of Appeal found that the Revenue and Taxation Code (R&TC) Section 24402 deductible dividend provision discriminated against interstate commerce in violation of the Commerce Clause of the United States Constitution. R&TC Section 24402 provided for a deduction to the extent that the dividend payer was taxable in California. A statute that is held to be unconstitutional is invalid and unenforceable. Therefore, the deduction is not available.

The Unitary Method

Corporations deriving income from sources both within and outside California are required to measure their tax liability by income derived from, or attributable to, sources within California. To determine the portion of total income that is attributable to this state, California utilizes the unitary business principle. This concept has been validated by income and franchise tax cases for more than 80 years.

Under the unitary method, as applied by California, all of the elements comprising a single trade or business are viewed as a whole or unit, hence the term "unitary." The business income from all activities of a unitary business is combined into a single report, whether such activities are conducted by divisions of a single corporation or by members of a commonly controlled group of corporations. For most businesses, the combined business income is apportioned to California by a formula derived from the Uniform Division of Income for Tax Purposes Act (UDITPA) under R&TC Sections 25120-25139. The elements required in a combined report are discussed in detail beginning on page 4.

Development of the Unitary Method

The theory underlying the unitary business principle has its roots in property tax law, where the issue of apportionment arose during the 1870s in the context of railroad taxation (*State Railroad Tax Cases* (1876) 92 U.S. 575). A broader application later evolved as the states adopted the practice of measuring taxes by income. As early as 1920, the United States Supreme Court approved the use of a formula to apportion the income of a single corporation among several states in the case of *Underwood Typewriter Co. v. Chamberlain* (1920) 254 U.S. 113.

California's use of formula apportionment dates to 1929 and the enactment of the original Franchise Tax Act. The use of the unitary method to combine the income from unitary divisions of a single corporation was validated by the California Supreme Court in *Butler Bros. v. McColgan* (1941) 17 Cal.2d.664. In *Edison California Stores v. McColgan* (1947) 30 Cal.2d.472, the California Supreme Court extended the unitary business concept to allow apportionment of combined income of a common business activity conducted by a multi-corporate group.

While R&TC Section 25101 provides the general authority for use of the unitary business concept, no statutes have ever been adopted to define precisely the scope of application of the unitary principle. Instead, the law has evolved through a series of judicial decisions. For example:

- In *Superior Oil Co. v. Franchise Tax Board* (1963) 60 Cal.2d 406, the California Supreme Court held that once it is determined that a business with income from sources within and outside the state is unitary, formula apportionment MUST be utilized.
- The United States Supreme Court found California's application of the unitary business principle to multiple corporations to be constitutional in *Container Corporation v. Franchise Tax Board* (1983) 463 U.S. 159, aff'g 117 Cal. App.3d 988 (1981).
- Application of the unitary method is required whether the unitary business is carried on over state or international boundaries. Application of the unitary method to worldwide activities of a single corporation was first sanctioned by the United States Supreme Court in *Bass, Ratcliff & Gretton Ltd. v. State Tax Commission* (1924) 266 U.S. 271. More recent decisions upholding the application of the unitary method to worldwide activities of multiple corporations are *Container Corporation v. Franchise Tax Board*, discussed above; *Barclays Bank Internat., LTD v. Franchise Tax Board* (1994) 129 L. Ed 2d. 244; and *Colgate-Palmolive v. Franchise Tax Board* (1994) 129 L. Ed 2d. 244.

Tests for Determining Unity

Both *Butler Bros.* and *Edison California Stores*, discussed previously, set forth tests to be used in determining whether the activities of several divisions or corporations should be considered unitary. In *Butler Bros.*, the court held that a "unitary business" exists where there is: (1) unity of ownership; (2) unity of operation as evidenced by central divisions for functions such as purchasing, advertising, accounting, and management; and (3) unity of use in its centralized executive force and general system of operations. In *Edison California Stores*, the court held that if the operation of the portion of the business done within the state is dependent upon or contributes to the operation of the business outside the state, the operations are unitary.

The three unities test and the contribution or dependency test have been applied by the California courts in a variety of cases. (See, e.g., *Superior Oil Co. v. Franchise Tax Board* (1963) 60 Cal.2d 406, 411-412; *Honolulu Oil Corp. v. Franchise Tax Board* (1963) 60 Cal.2d 417, 423-424; *John Deere Plow Co. v. Franchise Tax Board* (1951) 38 Cal.2d 214, 221-222; *Container Corporation of America v. Franchise Tax Board* (1981) 117 Cal.App.3d 988, 994-1001, aff'd 463 U.S. 159, (1983); *Chase Brass & Copper Co. v. Franchise Tax Board* (1970) 10 Cal.App.3d 496, 501-502.) If either the three unities test or the contribution/dependency test is satisfied, the businesses are unitary (*A.M. Castle & Co. v. Franchise Tax Board* (1995) 36 Cal. App. 4th 1794.)

The United States Supreme Court has also referred to a unitary business as one that exhibits "contributions to income resulting from functional integration, centralization of management, and economies of scale." (*Mobil Oil Corp. v. Comm'r of Taxes of Vt.* (1980) 445 U.S. 425, 438; *F. W. Woolworth Co. v. Taxation and Revenue Dep't of the State of N.M.* (1982) 458 U.S. 354, 366; *Allied Signal v. Director, Taxation Division* (1992) 504 U.S. 768.) That court further noted that, "[t]he prerequisite to a constitutionally acceptable finding of a unitary business is a flow of value, not a flow of goods." (*Container Corp. of America v. Franchise Tax Board* (1983) 463 U.S. 159, 178.) The Supreme Court has stated that for commonly controlled activities to be nonunitary, they must be part of "unrelated business activity which constitutes a 'discrete business enterprise.' (*Mobil Oil Corp.*, supra, 445 U.S. at 439-440.)

Cal. Code Regs., tit. 18 section 25120 provides additional rules and examples regarding what constitutes a unitary business. The regulation: (1) recognizes that a single taxpayer may have more than one "trade or business"; and (2) sets forth three factors, the presence of any one of which creates a "strong presumption" that the activities of the taxpayer constitute a single trade or business. Cal. Code Regs., tit. 18 section 25120 provides in pertinent part:

> (b) Two or More Businesses of a Single Taxpayer. A taxpayer may have more than one "trade or business." In such cases, it is necessary to determine the business income attributable to each separate trade or

business. The income of each business is then apportioned by an apportionment formula which takes into consideration the in-state and out-of-state factors, which relate to the trade or business, the income of which is being apportioned.

The determination of whether the activities of the taxpayer constitute a single trade or business, or more than one trade or business, will turn on the facts in each case. In general, the activities of the taxpayer will be considered a single business if there is evidence to indicate that the segments under consideration are integrated with, dependent upon, or contribute to each other and the operations of the taxpayer as a whole. The following factors are considered to be a good indication of a single trade or business, and the presence of any of these factors creates a strong presumption that the activities of the taxpayer constitute a single trade or business:

(1) Same type of business – This factor applies when all of a taxpayer's activities are in the same general line, such as in the operation of a chain of retail grocery stores.

(2) Steps in a vertical process – An example of this factor would be a taxpayer that explores for and mines copper ores; concentrates, smelts, and refines the copper ores, and fabricates the refined copper into consumer products.

(3) Strong centralized management – A taxpayer that might otherwise be considered as engaged in more than one trade or business is properly considered as engaged in one trade or business when there is a strong central management, coupled with the existence of centralized departments for such functions as financing, advertising, research, or purchasing.

For court decisions that discuss strong centralized management and the application of the unitary concept to diverse businesses, see *Mole-Richardson Co. v. Franchise Tax Board* (1990) 220 Cal.App.3d 889, 894; *Tenneco West, Inc. v. Franchise Tax Board* (1991) 234 Cal.App.3d 1510 and *Dental Insurance Consultants, Inc. v. Franchise Tax Board* (1991) 1 Cal.App.4th 343. For application of the unitary tests to passive holding companies, see FTB Legal Rulings 95-7 and 95-8, dated November 29, 1995.

As noted above, the activities of a single corporation or group of commonly owned corporations do not always constitute a single unitary business. If a taxpayer has two or more trades or businesses that are not unitary with one another, separate combined report computations must be made to compute business income and apportionment factors for each trade or business and to apportion to California the business income of each.

California law classifies income as either "business" or "nonbusiness." Business income is income arising from transactions and activity in the regular course of the taxpayer's trade or business. Business income includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer's regular trade or business operations. Business income is assigned through formula apportionment, R&TC Section 25120(a). Nonbusiness income is all other income, R&TC Section 25120(d), and is generally allocated to a particular jurisdiction (R&TC Sections 25123-25127). Regulations under R&TC Section 25120 also provide guidance for distinguishing between business and nonbusiness income. For further discussion and examples of business and nonbusiness income, refer to the instructions for Schedule R, Apportionment and Allocation of Income.

Unity of Ownership

A corporation may file a combined report with other members of a unitary group only if the corporations are members of a commonly controlled group as defined by R&TC Section 25105. Generally, a commonly controlled group exists when stock possessing more than 50% of the voting power is owned, or constructively owned, by a common parent corporation (or chains of corporations connected through the common parent) or by members of the same family. A commonly controlled group also includes corporations that are stapled entities, see R&TC Section 25105(b)(3). Special rules are provided in R&TC Section 25105 for partnerships, trusts and transfers of voting power by proxy, voting trust, written shareholder agreement, etc.

The Use of a Combined Report

Two or more corporations conducting a unitary business within and outside California are required to use the combined reporting approach to determine California source income subject to tax by California.

R&TC Section 25101.15 allows corporations conducting a unitary business wholly within California to file a combined report.

A corporation that has made a valid election to be treated as an "S corporation" may not generally be included in a combined report. However, in some cases, the FTB may use combined reporting methods to clearly reflect income of an S corporation, R&TC Section 23801(d)(1).

The combined report is a means by which the income of a unitary business is divided among the taxing jurisdictions in which the trade or business is conducted. A combined report is not a "return," but merely the name given to the calculations by which multi-entity unitary businesses apportion income on a geographic basis. There is no "combined report" form; tax is calculated on an attachment to Form 100 or Form 100W using the format described in this publication.

In a combined report, the entire amount of unitary business income of all corporations in the unitary group (including unitary members with no property, payroll, or sales within California) is aggregated in the combined report.

The combined business income of the unitary group is then apportioned to California and to the unitary members subject to tax in California. Details of this formula are discussed in the instructions to Schedule R, Apportionment and Allocation of Income. Refer to R&TC Sections 25129 through 25137, the corresponding regulations and FTB Notice 2004-5 for guidelines on calculating the apportionment formula. The process of apportioning the combined business income to the taxpayer members of the group is commonly referred to as "intrastate apportionment." The rules for those computations are provided in Cal Code Regs., tit. 18 section 25106.5(c)(7). The California net income of each member is then computed, taking into account its apportioned share of the unitary group business income or loss plus any income from a business wholly conducted in California, California source nonbusiness income or loss, and allowable California source net operating loss. Unless otherwise provided by statutory authority, credits are applied against the tax on a separate entity basis and specific credit(s) are only available to the taxpayer corporation that incurred the expense that generated the credit(s). Unlike a consolidated return, in which the group is treated as a single taxpayer, members of a unitary business are taxed individually and each affiliate doing business, qualified to do business, or incorporated in California is subject to at least the minimum franchise tax. Generally, each California taxpayer included in the combined report must file its own tax return using Form 100 or Form 100W. However, some unitary groups may elect to file a single group Form 100 or Form 100W and report the sum of the separate tax liabilities of the unitary members. See Schedule R-7 of Schedule R, Apportionment and Allocation of Income.

Contents of a Combined Report

A combined report should contain all of the following:

- A list of subsidiaries/affiliates and their California corporation numbers and FEINs.
- A combined profit and loss statement in column format disclosing each corporation's statement of profit and loss.
- A schedule in column format disclosing the various adjustments for each corporation necessary to convert the combined profit and loss statement to the combined income subject to apportionment. This schedule includes any adjustments necessary to revise federal or foreign income to that reported for California purposes, as well as adjustments for income from a separate trade or business or for nonbusiness income or loss.
- A combined apportionment formula in column format disclosing for each corporation the total amount of property, payroll, and sales, and the amount of California property, payroll, and sales.
- A schedule in column format disclosing for each corporation any items of nonbusiness income or expense allocated to California.
- Schedules disclosing the computation of the charitable contributions adjustment.
- A schedule in column format of the alternative minimum tax calculation for each corporation.
- Schedules in column format disclosing for each corporation all data required by Form 100 or Form 100W. These schedules include:
  1. Balance sheets.
  2. Gains and losses from sale or exchange of assets.
  3. Taxes on or measured by income.
  4. Dividends and interest received.
  5. Income or loss from rentals, royalties, partnerships, and miscellaneous sources.
  6. Net operating losses.

- Schedules in column format showing the computation of income apportionable and allocable to this state for each member of the group, and the computation of each member's tax credits and tax liability.

A comprehensive example illustrating the use of the above schedules begins on page 10.

Consolidated Return Distinguished From a Combined Report

Unless specifically stated otherwise, California does not follow the federal consolidated return regulations provided under Internal Revenue Code (IRC) Section 1502. With respect to earnings and profits (E&P) and stock basis, California has no provisions similar to the investment adjustments allowed for federal purposes under Treas. Reg. Sections 1.1502-32 and -33. The E&P of each entity in the combined report is calculated on a separate accounting basis and does not include the E&P of any lower tier subsidiaries (see *Appeal of Young's Market Company*, Cal. St. Bd. of Equal., 11/19/86). Likewise, the cost basis of a unitary subsidiary's stock is not adjusted to reflect the E&P of that subsidiary (see A*ppeal of Safeway Stores, Cal. St. Bd. of Equal.*, 3/2/62 and *Appeal of Rapid American Corp.* Cal. St. Bd. of Equal., 10/10/96).

S Corporations

If an S corporation holds 100% of the stock of a subsidiary, and elects to treat that subsidiary as a qualified subchapter S subsidiary (QSub), then a combined return is not filed. Instead, the QSub is disregarded, and the activities, assets, liabilities, income, deductions, and credits of the QSub are treated as activities, assets, liabilities, income, deductions, and credits of the S corporation parent. If the QSub is not unitary with the S corporation, then it is treated as a separate division and separate computations must be made to compute business income and apportionment factors for the QSub and the S corporation, and to apportion to California the business income of each.

Corporations With Different Accounting Periods

Common Accounting Period Necessary
When filing a combined report, each member must align its income and apportionment data from its own accounting period to the accounting period of the "principal member." Where there is a parent-subsidiary relationship in the combined reporting group, the parent corporation will generally be the principal member. If there is no corporation in the combined reporting group which is a parent corporation to all the other members, the principal member will be the member that is expected to have, on a recurring basis, the largest value of real and tangible personal property in California as determined for property factor purposes. However, the taxpayer members of a combined reporting group may elect to treat any other member of the combined reporting group as the "principal member." Once the election is made in the first year that a combined report is required, the principal member may only be changed with the consent of the FTB. See Cal Code Regs., tit. 18 section 25106.5(b)(12).

Income Calculation
Each member of the group should generally use the actual figures taken from its books to determine the proper income and related computations corresponding to the accounting period of the principal member. This will usually require an interim closing of the books for members whose normal accounting period differs from the accounting period of the principal member. Alternatively, a pro-rata method of converting income to the principal member's accounting period will be accepted as long as the results do not produce a material misstatement of income apportioned to the state (see Cal. Code Regs., tit. 18 section 25106.5-4(c)).

Pro-Rata Method
Under the pro-rata method, income of a member of the group is converted to the accounting period of the principal member on the basis of the number of months falling within the applicable taxable year. For example, if a parent corporation operates on a calendar year basis and a subsidiary to be included in a combined report operates on a September 30 taxable year, it is necessary to assign 9/12 of the subsidiary's unitary income of one taxable year and 3/12 of the unitary income of the succeeding taxable year to arrive at a full twelve months' income to be included in the combined report. Where this procedure results in using the income of a corporation whose taxable year has not yet closed, it may be necessary to make an estimate based on available information and amend the tax return at a later date.

Apportionment of Combined Unitary Income Using a Common Accounting Period
The factors of the combined formula should be computed on the basis of the same accounting period that was used to compute the unitary income. If an interim closing of the books was done to determine income attributable to the accounting period of the principal member, then the actual figures from the interim closing should be used to determine the apportionment factors as well. If the pro-rata method is used to convert income, then a pro-rata method should also be used to convert the factors of a member of the group to the accounting period of the principal member.

Once income and apportionment factors have been placed on a common accounting period, combined unitary business income is apportioned to California and to each of the taxpayer member corporations filing returns in California. For each California reporting corporation with a normal accounting period that differs from the accounting period of the principal member, the California income apportioned to that corporation is then converted back to the corporation's normal accounting period. This conversion is made on the basis of the number of months falling within the common taxable year of the group.

The computations necessary to determine the combined income under the pro-rata method, when members of the group are on different accounting periods, are illustrated in the example beginning on page 10 of this publication. For more information, see Cal. Code Regs., tit. 18 section 25106.5-4.

Part-Year Members

A part-year member is a corporation that either becomes a member, or ceases to be a member of the unitary group, after the beginning of the taxable year. If the part-year member is required to file two short period returns for the taxable year, then the income for the period in which the member was unitary with the group must be determined on a combined basis. The income for the remaining short period will be determined on a separate basis (or on a combined basis with a different group if the taxpayer had a unitary relationship with one or more corporations in that short period).

If the part-year member is **not** required to file short period returns, then it must file a single return for the entire year. The income reported on that return would be determined by combined reporting procedures for any period in which the part-year member was part of a unitary group, and by separate accounting for any period it was not part of a unitary group. Use the actual income and apportionment data from the common unitary period to apportion income for that period. See the interim closing discussion under "Apportionment of Combined Unitary Income Using a Common Accounting Period." However, the comprehensive example beginning on page 10 contains an acceptable pro-rata method for this computation, if that method does not cause income apportioned to this state to be materially misstated. For more information, see Cal. Code Regs., tit. 18 section 25106.5-9.

R&TC Section 24632 provides that the taxable year of a taxpayer may not be different than the taxable year used for purposes of the IRC, unless initiated or approved by the FTB. Whenever a taxpayer is required to file a federal return for a period of less than 12 months, a California return for that period is also required. Federal due dates for these short period returns also apply for California.

Adjustments for Intercompany Transactions

Intercompany Sales
Cal. Code Regs., tit. 18 section 25106.5-1 provides detailed rules relating to the treatment of intercompany transactions between members of a combined reporting group. These regulations apply to intercompany transactions that occur on or after January 1, 2001.

In general, the regulations adopt the treatment of intercompany transactions for federal consolidated return purposes (Treas. Reg. Section 1.1502-13). Under those regulations, income from intercompany transactions is generally deferred until immediately before such time that:

1) The asset leaves the group by a sale or other disposition to a nonmember.
2) The buyer and the seller no longer constitute members of the same combined reporting group, including by means of a water's-edge election.
3) The purchaser converts the asset to a nonbusiness use.

When income from a deferred intercompany transaction is required to be restored, it is apportioned using the apportionment percentages of the members of the group for the taxable year in which the income is restored. Special rules apply for “partially included water's-edge corporations” described by R&TC Sections 25110(a)(4) and (a)(6).

A taxpayer may elect to report income from an intercompany transaction in the year in which that transaction occurred, if it has made a similar election under Treas. Reg. Section 1.1502-13(e), or in the event that regulation does not apply, if the intercompany transaction was reported as current taxable income in the year of the intercompany sale for federal or foreign national tax purposes.

Intercompany Distributions in Excess of Stock Basis

Income from an intercompany distribution between members of a combined reporting group that exceeds the payor's E&P and stock basis, described by IRC Section 301(c)(3), is deferred. That income is restored to the extent that the holder of the stock disposes of its stock, even if the distributor remains in the holder's combined reporting group. If the distributor liquidates into the distributee, the deferred income is taken into account ratably over 60 months, unless the taxpayer elects to take such income into account in full in the year of the liquidation.

Effect of Intercompany Transactions on Apportionment Factors

Intercompany transactions are disregarded for purposes of the property factor. The purchaser takes the seller's original cost, prior to the intercompany transaction, so long as the seller and purchaser remain in the same combined reporting group. If the purchaser and the seller leave the same combined reporting group, resulting in a restoration of deferred income, the property factor is adjusted to reflect the purchaser's original cost. Intercompany rents are also disregarded for purposes of the property factor.

Intercompany transactions are disregarded for purposes of the sales factor, even if income from an intercompany transaction is required to be restored as a result of the purchase and the seller leaving the same combined reporting group. If an asset that was sold in an intercompany transaction is later sold to a nonmember, the gross receipt from the sale to the nonmember is reflected in the sales factor of the intercompany purchaser.

Dividends

To the extent that intercompany dividends are paid out of E&P derived from unitary business income, they are eliminated in computing the California measure of tax (R&TC Section 25106). In determining whether a dividend is paid out of unitary E&P, distributions are deemed to be paid first out of current E&P and then out of prior years' accumulation in reverse order of accumulation. Distributions paid out of nonbusiness E&P, or distributions from E&P accumulated prior to the time the payer corporation became a member of the combined group, are not eliminated from the income of the recipient corporation (although such dividends may be subject to deduction under R&TC Section 24411).

Intercompany Transactions Prior to January 1, 2001

Intercompany transactions which occurred before January 1, 2001, are governed by pre-existing practices, even if, in a later year, the asset which was the object of an intercompany transaction is later resold to a nonmember or the seller and the purchaser discontinue their combined reporting relationship. Accordingly, the prior practices of the FTB are reproduced here.

Summary of Prior Practices

The following guidelines reflect the FTB's policy regarding adjustments necessary to properly reflect intercompany transactions among unitary affiliates included in the combined report that occurred in taxable years beginning before January 1, 2001.

- **Inventories**
  Income from intercompany sales of inventory is eliminated from unitary business income. The seller's basis in the inventory will carry over to the buyer in the intercompany sale. Intercompany profits in inventory shall be eliminated for property factor purposes.
- **Intangible Assets**
  Gain or loss from intercompany sales of intangible assets shall be eliminated from unitary business income. The seller's basis in the intangible assets will carry over to the buyer in the intercompany sale.
- **Fixed Assets and Capitalized Items**
  The gain or loss on intercompany sales of business fixed assets or capitalized intercompany charges and expenditures between members of a combined group are generally deferred. The exception to this rule occurs when an affiliated group that files a consolidated federal return elects not to defer gain or loss on intercompany transfers. In that case, the federal election will be allowed for the combined report.

  Under the general rule, the gain or loss remains deferred as long as both the seller and the purchaser remain in the combined group and the asset is not sold to outsiders. When either the seller or purchaser is no longer a member of the combined group, or the group for any reason terminates combined reporting, the gain or loss is reportable by the seller at a time immediately preceding the date either corporation ceases to be a member of the group. If the asset is sold to a third party, the deferred gain or loss is reportable by the combined group in the year of sale. A water's-edge election is also a restoration event which will cause previously deferred intercompany gains and losses to be included in income on a pro-rata basis over five years (refer to FTB Notice 89-601 for further details of this computation). The amount of gain recognized upon the occurrence of a restoration event is generally the same amount that would be reportable for federal purposes under similar circumstances in a consolidated return.

  Where intercompany gain or loss is deferred, the basis of the asset for property factor purposes shall be the seller's cost.
- **Other Factor Adjustments**
  For factor purposes, intercompany sales and other intercompany revenue items are eliminated in computing the numerator and denominator of the sales factor. Intercompany rent charges are also eliminated from the property factor computation.

Unitary Partnerships

When a corporation is a partner in a partnership and the partnership's activities are unitary with the corporation's activities (disregarding ownership requirements), then the corporation's share of the partnership's trade or business is combined with the corporation's trade or business (see Cal. Code Regs., tit. 18 section 25137-1).

For example, assume that Corporation A has a 20% partnership interest in Partnership P and that the activities of Corporation A and Partnership P are unitary. The unitary business is required to double weight the sales factor under R&TC Section 25128.The apportionment factors for A and P are as follows:

Apportionment Factors of a Corporation and a Unitary Partnership

	EVERYWHERE		CALIFORNIA	
	Corporation A	Partnership P	Corporation A	Partnership P
Property	400,000	250,000	300,000	75,000
Payroll	100,000	50,000	50,000	25,000
Sales	500,000	300,000	400,000	100,000

Corporation A's 20% share of Partnership P's property, payroll, and sales is included in the combined apportionment factor.

		EVERYWHERE	CALIFORNIA	FACTOR
Combined Property:	Corporation A	400,000	300,000	
	Partnership P (20%)	50,000	15,000	
	Combined	**450,000**	**315,000**	**70%**
Combined Payroll:	Corporation A	100,000	50,000	
	Partnership P (20%)	10,000	5,000	
	Combined	**110,000**	**55,000**	**50%**
Combined Sales:	Corporation A	500,000	400,000	
	Partnership P (20%)	60,000	20,000	
	Combined	**560,000**	**420,000**	**75%**
	Combined x 2			**150%**
Apportionment % (70+50+150)÷4				**67.5%**

Assume that the net business income for Corporation A and Partnership P was $300,000 and $100,000 respectively. Assuming that Corporation A's distributive share of partnership P's profits and losses was also 20%, Corporation A's net income apportioned to California would be:

Corporation A's net business income	$300,000
Corporation A's distributive share of Partnership P's net business income ($100,000 x 20%)	20,000
	320,000
Multiplied by combined apportionment factor (from above)	x 67.5%
Corporation A's net income apportioned to California	$216,000

Net Operating Losses (NOLs)

For taxable years beginning on or after January 1, 2004, California has reinstated the Net Operating Loss (NOL) carryover deductions.

For taxable years that began in 2002 and 2003, California suspended the NOL carryover deduction. Taxpayers continued to compute and carryover an NOL during the suspension period. However, the deduction for disaster losses was not affected by the NOL suspension rules.

The carryover period for suspended losses is extended by two years for losses incurred before January 1, 2002, and by one year for losses incurred after January 1, 2002, and before January 1, 2003. For more information get form FTB 3805Q, Net Operating Loss (NOL) computation and NOL and Disaster Loss Limitations — Corporations.

California incorporates, with specific modifications, the provisions of IRC Section 172, concerning carryovers of NOLs incurred in the conduct of a trade or business. In general, California law allows 50% of the NOLs incurred during taxable years beginning on or after January 1, 1987, and before January 1, 2000, to be carried forward for up to five years.

For taxable years beginning on or after:

- January 1, 2004, 100% of the NOL may be carried forward.
- January 1, 2002, and before January 1, 2004, 60% of the NOL may be carried forward.
- January 1, 2000, and before January 1, 2002, 55% of the NOL may be carried forward.

Also, any NOL incurred in any taxable year beginning on or after January 1, 2000, may be carried forward for ten years.

For taxable years beginning on or after January 1, 1994, and before January 1, 2000, new businesses may carry over 100% of the NOL incurred during the first three years of operation. The carryover period is eight years for losses incurred in the first taxable year of business, seven years for losses incurred in the second year of business, and six years for losses incurred in the third year. For taxable years beginning on or after January 1, 2000, new businesses may carry over 100% of the NOL incurred during the first three years of operation. The carryover period is ten years.

In addition, small businesses may carry over 100% of an NOL incurred during taxable years beginning on or after January 1, 1994. The carryover period is five years. For taxable years beginning on or after January 1, 2000, the carryover period is ten years. A small business is a business with total receipts of less than $1 million during the taxable year.

For more information regarding "eligible small business" and "new business" NOLs, get FTB Legal Ruling 96-5.

California does not have a provision that allows NOL carrybacks.

For taxable years where the taxpayer has a water's-edge election in effect, the deduction of an NOL carryover is not allowed to the extent that such NOL was determined by taking into account the income and factors of a corporation that would not have been included in the combined report if a water's-edge election had been in effect in the year in which the loss was incurred.

Further information regarding the general NOL carryover can be found in form FTB 3805Q. California also has special NOL provisions for losses incurred in farming businesses affected by Pierce's disease, Enterprise Zones, the Los Angeles Revitalization Zone, Targeted Tax Areas, and Local Agency Military Base Recovery Areas. For more information regarding these NOLs, see R&TC Sections 24416 through 24416.7, and/or get form FTB 3805D, NOL Computation – Pierce's Disease; form FTB 3805Z, Enterprise Zone Business Booklet; form FTB 3806, Los Angeles Revitalization Zone Business Booklet; form FTB 3807, Local Agency Military Base Recovery Area Business Booklet; and form FTB 3809, Targeted Tax Area Business Booklet.

Application of NOL Carryovers in a Combined Report

The NOL for each taxpayer in the combined group is computed by determining each taxpayer's share of the unitary business income or loss and then adjusting for any nonbusiness income or loss of this taxpayer. In a subsequent year, when a member of the group has positive California net income (from either unitary business or nonbusiness income), only the amount of NOL **attributable to that particular taxpayer** may be deducted. The example on the next page shows the computations involved in determining and applying an NOL in a combined report. See Cal. Code Regs., tit. 18 section 25106.5(e).

Another example of an NOL is shown in Schedule 5-F in the comprehensive example on page 23 of this booklet. Although unitary business income apportioned to each taxpayer in that example was positive, a nonbusiness loss caused Corporation C to have a net loss for California. 100% of that loss will be available to be carried forward to subsequent years, although a deduction will be allowed only from California net income apportioned or allocated to Corporation C.

Applying an NOL in a Combined Report

YEAR 1:	Corp. X	Corp. Y	Corp. Z	Combined
Unitary business income (loss) subject to apportionment	(400,000)	(10,000)	60,000	(350,000)
Apportionment percentages	5%	1%	3%	9%
Loss apportioned to California (Combined loss x %)	(17,500)	(3,500)	(10,500)	(31,500)
Nonbusiness items wholly attributable to California	50,000	(2,500)	0	
California net income (loss)	32,500	(6,000)	(10,500)	
NOL available to be carried forward (100% of loss)	0	(6,000)	(10,500)	

YEAR 2:	Corp. X	Corp. Y	Corp. Z	Combined
Unitary business income (loss) subject to apportionment	50,000	80,000	(5,000)	125,000
Apportionment percentages	6%	4%	4%	14%
Income apportioned to California (Combined income x %)	7,500	5,000	5,000	17,500
Nonbusiness items wholly attributable to California	2,500	(10,000)	0	
California net income (loss)	10,000	(5,000)	5,000	
Application of NOL carryover from Year 1	0	0	(5,000)	
California net income (loss)	10,000	(5,000)	0	
NOL available to be carried forward (100% of loss)	0	(5,000)	0	

	Corp. X	Corp. Y	Corp. Z
Remaining NOL from Year 1	0	(6,000)	(5,500)
Loss in Year 2	0	(5,000)	0
NOL available to be carried forward	0	(11,000)	(5,500)

Capital Loss Limitation

California conforms to the federal provisions for netting gains and losses from involuntary conversions, Section 1231 assets, and capital assets. If the netting process results in net capital losses, the losses are not deductible in the current year, but may be carried over to subsequent years. In a combined reporting group, the members' business gains and losses in each class (i.e., the classes are involuntary conversion, 1231, short-term capital or long-term capital) are combined (without netting between classes), and each taxpayer member determines its share of the business gain/loss items in each class based on its apportionment percentage. Then, each taxpayer member applies the federal netting rules to its post-apportioned share of business gain/loss items and its California-source nonbusiness gain/loss items. If a net loss results for any taxpayer member, it may be carried forward by that member for up to five years. For more information regarding the application of the capital loss limitation in a combined report, see Cal. Code Regs., tit. 18 section 25106.5-2.

The forms used to compute gains and losses from involuntary conversions, Section 1231 assets and capital assets, are the federal Form 4684, Casualties and Thefts; California Schedule D-1, Sales of Business Property; and California Form 100 or Form 100W, Schedule D, Capital Gains and Losses.

Application of Capital Loss Limitation in a Combined Report

Members of a combined reporting group should complete a new federal Form 4684, California Schedule D-1, and California Schedule D for each member of the combined reporting group, as provided below. Be sure to compute gains and losses using California basis information under California law. Enter that member's separate entity data using California amounts, and identifying whether the items relate to business or nonbusiness income.

Also, prepare a schedule similar to that provided in the capital gain (loss) example on page 9, and in Schedule 5-E of the comprehensive examples starting on page 12.

Complete federal Form 4684, Section B only, through line 37, for each member of the combined reporting group, using that member's separate entity data. Any amounts entered on line 31 should be transferred to that member's Schedule D-1, line 14. Enter net business and California nonbusiness gain/loss data from lines 36 and 37 in the appropriate column of lines 1a and 1c in a format similar to the example that follows.

Complete California Schedule D-1, lines 1 and 2, and 4-6 for each member of the combined reporting group. Do not enter data on line 3. Combine and enter business and California nonbusiness data from those lines in the appropriate column of lines 2a and 2c in a format similar to the example that follows. Do not enter data on lines 7-9 or 11-12 of Schedule D-1. The remaining portion of Schedule D-1 should be completed for each member of the combined reporting group using separate entity data.

Gains (losses) reported on the Schedule D-1 on lines not specifically referenced above or included in the capital gain (loss) example are not included in the capital loss limitation calculation. These amounts are included in federal income before state adjustments and should not be removed from income prior to apportionment.

Complete California Form 100 or Form 100W, Schedule D for each member of the combined reporting group, using that member's separate entity data. Do not enter data on Schedule D, lines 3 or 9 through 11. Enter the amounts from Schedule D, line 4 in the appropriate column of lines 3a and 3c in a format similar to the example that follows. Do not enter any other data from Schedule D-1 on Schedule D, line 6; enter only amounts from capital gain distributions, if any. Enter the amounts from Schedule D, line 8 in the appropriate column of lines 4a and 4c in a format similar to the example that follows.

If the combined reporting group uses the members' federal return(s) as the starting point for the computation of California income, certain items included in federal taxable income should be revised. For example:

- Casualty or theft loss (line 38a of federal Form 4684).
- Section 1231 (federal Form 4797, line 11) or
- Net capital gain (federal Form 1120, Schedule D, line 13).

These items should be reversed as a California addition or subtraction adjustment on Schedule 1B of the comprehensive example. Additional adjustments resulting from federal/state differences in the use of federal Form 4684 for California purposes, in the California Form 100, Schedule D and in the California Schedule D-1 may also be appropriate, and should likewise be entered as a California adjustment on Schedule 1B of the comprehensive example.

The following example provides the format to use to calculate the capital loss limitation. In this example, all figures carried from federal Form 4684, California Schedule D-1, and California Schedule D are assumed. The California apportionment percentages shown at the top of the schedule for this example are assumed values. Those percentages would have been calculated in a schedule comparable to Schedule 5-D of the comprehensive example.

Capital gain (loss) example

Capital loss limitation schedule	A	B	C	Total
CA Apportionment percentage. See instructions	20%	30%	10%	60%
1. Reference: Federal Form 4684, Lines 36 and 37.				
1a. Net business casualty/theft gain or loss (Combine business amounts on lines 36 and 37, from federal Form 4684)	0	15,000	0	15,000
1b. California apportioned casualty/theft gain or loss (Line 1a total x member's CA apportionment percentage)	3,000	4,500	1,500	9,000
1c. Net California nonbusiness casualty/theft gain or loss (Combine nonbusiness amounts on lines 36 and 37, from federal Form 4684)	0	0	0	0
1d. Net California source casualty/theft gain or loss (combine lines 1b and 1c) If a net loss, enter on line 6a. If a net gain, enter on line 2d.	3,000	4,500	1,500	9,000
2. Reference: California Schedule D-1, Lines 6-8.				
2a. Net business Section 1231 gain/loss (Combine business amounts on lines 2, 4, 5, and 6, California Sch. D-1)	75,000	20,000	30,000	125,000
2b. California apportioned Section 1231 gain/loss (Line 2a total x member's CA apportionment percentage)	25,000	37,500	12,500	75,000
2c. Net California nonbusiness Section 1231 gain/loss (Combine nonbusiness amounts on lines 2, 4, 5, and 6, California Sch. D-1)	0	0	0	0
2d. California casualty/theft gain (from line 1d)	3,000	4,500	1,500	9,000
2e. Net California source Section 1231 gain/loss (Combine lines 2b, 2c, and 2d) If a net loss, enter amount on line 6b	28,000	42,000	14,000	84,000
2f. If amount on line 2e is a gain, enter nonrecaptured Section 1231 losses (after apportionment and allocation) from prior years, if any	0	0	0	0
2g. Subtract line 2f from gain on line 2e, but if zero or less, enter -0-. If a net gain, enter amount on line 4d.	28,000	42,000	14,000	84,000
2h. If line 2e is a gain, enter the lesser of line 2f or the gain on line 2e here, and on line 6c. The remaining amount of line 2f, if any, is carried forward to subsequent years	0	0	0	0
3. Reference: California Schedule D, Form 100 or 100W, Part 1				
3a. Business net short-term capital gain/loss (Combine business amounts on lines 1 and 2, California Sch. D)	-20,000	-90,000	10,000	-100,000
3b. California apportioned net short-term capital gain/loss (Line 3a total x member's CA apportionment percentage)	-20,000	-30,000	-10,000	-60,000
3c. California nonbusiness net short-term capital gain/loss (Combine nonbusiness amounts on lines 1 and 2, California Sch. D)	10,000	0	20,000	30,000
3d. California source capital loss carryover from prior year	0	0	0	0
3e. California source net short-term capital gain/loss (Combine lines 3b, 3c, and 3d)	-10,000	-30,000	10,000	-30,000
4. Reference: California Schedule D, Form 100 or 100W, Part II, lines 5-7				
4a. Business net long-term capital gain/loss (Combine business amounts on lines 5 -7, California Sch. D)	200,000	-90,000	400,000	510,000
4b. California apportioned net long-term capital gain/loss (Line 4a total x member's CA apportionment percentage)	102,000	153,000	51,000	306,000
4c. California nonbusiness net long-term capital/gain loss (Combine nonbusiness amounts on lines 5 -7, California Sch. D)	0	0	0	0
4d. California source net Section 1231 gains (line 2g)	28,000	42,000	14,000	84,000
4e. California source net long-term capital gain/loss (Combine lines 4b, 4c, and 4d)	130,000	195,000	65,000	390,000
5. Reference: California Schedule D, Form 100 or 100W, Part II, lines 9-11				
5a. Excess of CA source net short-term capital gain over CA source net long-term capital losses (subtract loss on line 4e, if any, from gain on line 3e)	0	0	10,000	10,000
5b. Excess of CA source net long-term capital gains over CA source net short-term capital loss (subtract loss on line 3e, if any, from gain on line 4e)	120,000	165,000	65,000	350,000
5c. Net CA capital gain (add lines 5a and 5b). Enter here and on line 6d	120,000	165,000	75,000	360,000
5d. Net CA capital loss (Combine lines 3e and 4e.) If a net loss enter here. This is the member's CA source capital loss, and is carried forward to subsequent years	0	0	0	0
6. Reference: California Schedule R, line 32 (Post-apportioned amounts from capital gains (losses) netting)				
6a. Net CA source casualty loss (line 1d)	0	0	0	0
6b. Net CA source section 1231 loss (line 2e)	0	0	0	0
6c. CA source section 1231 gain recapture (line 2h)	0	0	0	0
6d. Net CA source capital gain (line 5c)	120,000	165,000	75,000	360,000
6e. Net post-apportioned amount from capital gains (losses) netting (Combine lines 6a through 6d, enter here, and on line 32 of California Schedule R)	120,000	165,000	75,000	360,000

Alternative Minimum Tax (AMT)

Generally, the calculation of alternative minimum taxable income (AMTI) incorporates the same concepts used in the calculation of regular California taxable income. The AMTI of the members of a combined group must therefore be allocated or apportioned to California and to each member in the same manner as is regular taxable income. The AMT NOL is computed based upon AMTI and is determined for each member of the combined group using the computations described on pages 7 and 8.

The calculation of AMTI includes an adjustment that represents 75% of the difference between the adjusted current earnings (ACE) of the corporation over the AMTI determined without regard to the ACE adjustment or the AMT NOL deduction (pre-adjustment AMTI). To compute this adjustment, the ACE of the members of a combined group must be allocated or apportioned in the same manner as regular taxable income and AMTI. Each taxpayer member must compare the ACE, after apportionment and allocation to California (California source ACE), with its pre-adjustment AMTI, after apportionment and allocation to California (California source pre-adjustment AMTI).

If California source ACE exceeds California source pre-adjustment AMTI (a positive ACE adjustment), 75% of the difference must be added to California source pre-adjustment AMTI. On the other hand, if California source pre-adjustment AMTI exceeds the ACE (a negative ACE adjustment), the negative adjustment may be applied to reduce California source pre-adjustment AMTI only to the extent that the aggregate positive California source ACE adjustments in prior years for that particular taxpayer member exceeded its aggregate negative ACE California source adjustments. See FTB Legal Ruling 94-3.

The computations necessary to calculate AMT for taxpayers in a combined report are shown in Schedule 6 of the comprehensive examples beginning on page 12 of this publication.

Election to File a Group Return

As a convenience, the FTB has adopted regulations under which some or all of the taxpayer members of a combined reporting group may elect to file a group return. See Cal. Code Regs., tit. 18 section 25106.5-11 for more information. The group return satisfies the requirement of each electing member to file its own return. The tax liability of each member of the unitary group must be computed using the combined reporting procedures described in this booklet. A separate computation of tax liability for each member of the group should be included with the group return. Each member incorporated, qualified to do business, or doing business in this state must pay at least the minimum franchise tax set forth in R&TC Sections 23153 and 23181. The tax liabilities of the electing group members are then aggregated and reported on the group return. Filing a group return does not change the tax liabilities of the taxpayer members.

The designated "key corporation" makes the election on behalf of itself and the electing members by completing Schedule R-7, Election to File a Unitary Taxpayers' Group Return and List of Affiliated Corporations, and attaching the schedule to the return. By filing a group return and the completed Schedule R-7, each electing member indicates acceptance of all terms and conditions set forth in the Schedule R-7 and instructions. The election is binding for the taxable year of the election and for all matters pertaining to the taxable year of the election.

To be eligible to make the election to file a group return, each corporation must: 1) be a member of a single unitary group for the entire taxable year; 2) have the same taxable year as the key corporation or the taxable year is wholly included within the taxable year of the key corporation; and 3) have the same statutory filing date as the key corporation for the taxable year.

If a corporation is not a member for the entire taxable year, they are not allowed to file a group return with the other members. Instead, the corporation files a separate return and attaches a copy of the combined report relating to all of the unitary members.

Identify each corporation in the group return by providing the complete legal name as registered with the California Secretary of State (SOS) for each corporation qualified to do business or incorporated in California and the California corporation number and federal employer identification number (FEIN). Do not use abbreviations unless the abbreviation is part of the corporation's legal name. This information should be provided on the Schedule R-7.

Exceptions — When A Group Return Is Not Allowed

Due to statutory filing requirements, California taxpayer corporations that have different accounting periods may not be included in a group return except as provided above. The business income of such corporations must be apportioned in accordance with the instructions for corporations that have different accounting periods (see page 5) and reported on a separate return.

Corporations may not file a group return if more than one unitary business is being conducted by any one taxpayer. For further information, get Schedule R, Schedule R-7, and their instructions.

Example of Combined Report Computations and Schedules

The following is an example of how the combined report approach is applied:

Corporations A, B, C, D, and E are engaged in a unitary business of manufacturing and selling items of tangible personal property. All members of the unitary group compute their separate entity income on a calendar year basis, except Corporation D, which uses a September 30 fiscal year end. The income and apportionment data for each of these corporations are reflected in the schedules that follow. Those schedules are explained in detail below. Additional facts that are specific to each member of the group follow:

Corporation A. Corporation A, a California domiciliary, is the parent corporation for the unitary group, and is the principal member of the group. Thus, all members of the combined reporting group must align their income and apportionment factors to Corporation A's calendar year for apportionment purposes.

Corporation A manufactures a product, some of which it sells to Corporation E. Corporations A and E use the first-in, first-out (FIFO) method of inventory accounting. In 2006, Corporation A sold $500,000 of product to Corporation E. The cost of goods sold for that sale was $400,000, resulting in an intercompany profit of $100,000. At the end of 2006, $200,000 in inventory purchased from Corporation A remained unsold in Corporation E's hands. Corporation A's remaining deferred intercompany income from those sales was $20,000. In 2007, Corporation E sold the remaining inventory it had purchased from Corporation A in the earlier year to an unrelated customer. In that same year, Corporation A sold additional product to Corporation E in the amount of $600,000. The cost of goods sold for that sale was $420,000, resulting in an intercompany profit of $180,000. At the end of the year, $100,000 in inventory remained unsold. Intercompany transactions are determined in accordance with Cal. Code Regs., tit. 18 section 25106.5-1 and are taken into account under the matching rule when there is a difference between the buyer's corresponding item and the recomputed corresponding item. For more information, see the section entitled "Adjustments for Intercompany Transactions" on page 5. Because Corporation E sold all of its inventory from year 2006 intercompany purchases from Corporation A, the amount of deferred income attributable to those sales that is required to be restored under the matching rule is $20,000. For the year 2007, the amount of deferred income attributable to intercompany sales is $180,000, of which $150,000 is required to be restored under the matching rule. Corporation A's remaining deferred intercompany income from those sales was $30,000. Thus, the net deferred income from intercompany transactions in 2006 and 2007 is $10,000 (see Schedule 1-C).

Corporation A has $100,000 interest income from its outstanding accounts receivable, $60,000 of which was attributable to California receivables. Losses of $100,000 were attributable to sales of obsolete equipment. The total gross receipts from the sales were $170,000, $68,000 of which were attributable to California. Corporation A received a $200,000 dividend from its unitary subsidiary, Corporation B. Because the dividend was paid from unitary earnings and profits accrued during a period in which Corporations A and B were in the same combined reporting group, the dividends are eliminated from income under R&TC Section 25106. In addition to income from its unitary business activity, Corporation A had dividend income of $150,000 from nonbusiness investments and a $30,000 partnership loss from a nonunitary oil and gas limited partnership operating entirely within California. The partnership had tax preference items for depletion and intangible drilling costs, of which Corporation A's distributive share was $40,000 and $10,000, respectively. After the tax preference items were applied, Corporation A's net AMTI attributable to the partnership was a positive $20,000 (see Schedule 6).

Corporation B. Corporation B operates entirely outside of California but has some mail order sales to California customers. This example assumes that Corporation B is not taxable in California. (For further discussion of taxability within the state, refer to FTB Pub. 1050, Application and Interpretation of Public. Law 86-272). Because Corporation B is not a California taxpayer, its sales to California are not assigned to this state. Corporation B also derives interest income from its outstanding accounts receivable. During the year, Corporation B sold a fixed asset to Corporation D for a sales price of $210,000 and a gain of $140,000. As explained in the section entitled "Adjustments for Intercompany Transactions" on page 5, the gain was deferred. Corporation B paid $10,000 of intercompany interest to Corporation C. The interest income is considered a current expense item to Corporation B and a current income item to Corporation C.

Corporation C. Sixty percent of the stock of Corporation C, was acquired by Corporation A on July 1 from an unrelated individual. Because of the economic relationship that existed prior to the acquisition, Corporation C became a member of the unitary group immediately upon acquisition. Because a short-period federal return was not required, Corporation C was not required to file a short-period return for California as a result of the acquisition but did an interim closing of its books on July 1. Corporation C has income from a California source based on the aggregate of its own income prior to acquisition, plus its apportioned share of the business income of the combined reporting group after the acquisition. Corporation C also has business rental income from leasing a portion of the ground floor of its headquarters to unrelated third parties. Corporation C was a limited partner in a nonunitary oil and gas partnership operated entirely within California and incurred a $150,000 partnership loss. The partnership had a December 31 year-end. The partnership had tax preference items for depletion and intangible drilling costs, of which Corporation C's distributive share was $200,000 and $15,000, respectively. After the tax preference items were applied, Corporation C's net AMTI attributable to the partnership was a positive $65,000 (see Schedule 6).

Corporation D. Corporation D computes its income on a September 30 fiscal year end. Because it is on a different accounting period than the principal member, Corporation A, it must fiscalize its income to the accounting period of Corporation A for purposes of the apportionment of income. Thus, a portion of its income from two separate accounting periods will be reflected in the combined report. Because Corporation D's income and apportionment factors remained stable throughout both periods, it is permitted to use the pro-rata method of fiscalization. After its income is apportioned to California, Corporation D must then prorate its apportioned share of the business income of the group back to its own respective accounting periods (see Schedule 3). Because Corporation D's return is due on December 15, it cannot include its tax liability in a group return filed by its parent, Corporation A, and must file its own return.

Corporation D purchased asset from Corporation B for $210,000 with an original cost basis of $70,000.

Corporation D also had a $100 tax credit carryover and a new tax credit of $125 for disabled access.

Corporation E. Corporation E was a member of the unitary group for the entire accounting period of Corporation A, the principal member. Corporation E purchased some of its inventory from Corporation A, a portion of which remained unsold at the end of the year. Corporation E also had a research and development tax credit in the amount of $2,000.

Corporation E sold business capital stock for $400,000 resulting in a gain of $100,000. Corporation E also had a California nonbusiness capital stock loss of $20,000.

The following schedules show the income computations for Corporations A, B, C, D, and E under the California combined reporting method:

Schedule 1: Combined income subject to apportionment.

For Corporations A, B, and E, this schedule reflects items of income and deduction for the calendar year ending 12/31/07. For Corporation C, only income and deductions incurred during the post-acquisition period of 7/1/07 through 12/31/07 are included in the combined report. Schedule 1-C shows the restoration and deferral of income from intercompany transactions.

Schedule 2: Corporation C's entire income for 2007.

Corporation C's income for its pre- and post-acquisition period are shown in Schedule 2. Only the post-acquisition income is included in the combined report.

Schedule 3: Computations to place Corporation D's income and apportionment factors on a calendar year basis.

If the interim closing-of-the-books method had been used to determine Corporation D's income for the 12/31/07 taxable year, then Corporation D's actual income for the calendar year would have been included in Schedule 1. In this example, however, Corporation D uses the pro-rata method of combining corporations with different accounting periods. Adjustments to convert Corporation D's income to the common year-end are shown on Schedule 3. The schedule calculates 9/12 of the income and deductions from the period ending 9/30/07, and 3/12 of the income and deductions from the period ending 9/30/08 to derive the income and deductions assigned to the 12/31/07 calendar year. The property, payroll, and sales are calculated and included in the same manner. Proration of Corporation D's share of the combined report business income back to Corporation D's accounting period is shown in Schedule 5-F.

Schedule 4: Calculation of combined interest offset.

The U. S. Supreme Court held California's interest offset provision, R&TC Section 24344(b), to be unconstitutional in circumstances in which non-business dividends or interest which are allocated outside of California exists within a unitary group (*Hunt-Wesson v. Franchise Tax Board* (2000) 120 S.Ct. 1022). As provided in FTB Notice 2000-9, the statute continues to apply for all corporations, to interest expense assigned to business interest income. For taxable years beginning on or after February 22, 2000, that portion of the interest offset that assigns interest expense to nonbusiness interest and dividend income shall apply only to interest expense assignable to nonbusiness interest and dividend income allocated to California.

Schedule 5: Combined apportionment formula and entity income assignment.

This schedule first computes the combined property, payroll, and sales within and outside California (Schedules 5-A through 5-C). For Corporation D, the property, payroll, and sales figures are from Schedule 3. On Schedule 5-D, the combined California apportionment percent is computed for each member, then multiplied by the combined unitary business income (from Schedule 1-B), to arrive at the member's combined business income apportioned to California. Each taxpayer member divides its own California property, payroll, and sales by the total property, payroll, and sales of the combined reporting group to compute its own California apportionment percentage. Corporation B is not a taxpayer and its sales are not reflected in the California numerator. On Schedule 5-F, Corporation A's share of California business income is adjusted by nonbusiness income attributable to California, and the interest offset is applied. The California business income of Corporation C is adjusted by its nonbusiness loss to derive its net income for state purposes for the period 7/1/07 through 12/31/07. This figure is combined with Corporation C's separate income for the period 1/1/07 through 6/30/07 (from Schedule 2) to arrive at Corporation C's net income for the entire calendar year. In this example, Corporation C has a net loss, 100% of which will be available to be carried forward and applied against Corporation C's California net income in subsequent years. The California business income assigned to Corporation D for the 2007 calendar year period is adjusted by 9/12 and is combined with 3/12 of the 2006 calendar year income (from the prior year combined reporting calculation) to arrive at Corporation D's net income for its 9/30/07 fiscal end period. California income subject to tax and the tax of each taxpayer member is shown on Schedule 5-F. The aggregate tax amount that would be reported on the group return would be $31,133 ($23,262 for Corporation A, and $7,871 for Corporation E). Only Corporation A and Corporation E may elect to file a group return. Neither Corporation C nor Corporation D is eligible to be included in a group return. Corporation C is a part-year member with net income including separate income from the pre-acquisition period, and Corporation D files its returns on a different year end from the remainder of the group. Corporation C and Corporation D must therefore file their own returns and include a copy of the combined report computations.

Schedule 6: Combined alternative minimum tax

The alternative minimum tax is computed using the combined reporting method. Schedule 6 shows the adjustments to combined reporting income to reflect the application of the alternative minimum tax, including adjustments attributable to adjusted current earnings (ACE). The alternative minimum tax amount is then carried into Schedule 5-F in the determination of each taxpayer member's respective tax liability.

SCHEDULE 1 – COMBINED INCOME SUBJECT TO APPORTIONMENT

1-A: COMBINED PROFIT & LOSS STATEMENT AS OF 12/31/07

	CORP A	CORP B	CORP C (7/1/07-12/31/07) (from Schedule 2)	CORP D (pro-rated from Sch. 3)	CORP E	TOTAL BEFORE ADJUSTMENT	DEFERRED INCOME and RESTORATION ADJUSTMENTS (from Schedule 1-C)	COMBINED
California ID number	7512345		7234567	7654321	7111111			
Federal ID number	62-3456789	62-7654321	61-2233445	22-11333445	69-9999999			
Net Sales	$7,000,000	$4,000,000	$1,900,000	$2,600,000	$2,600,000	$18,100,000		$18,100,000
Cost of goods sold	(5,900,000)	(2,500,000)	(1,000,000)	(1,500,000)	(1,600,000)	(12,500,000)		(12,500,000)
Gross profit	1,100,000	1,500,000	900,000	1,100,000	1,000,000	5,600,000		5,600,000
Deferred profit							(10,000)	(10,000)
Dividends	350,000					350,000		350,000
Interest on U.S. obligations						0		0
Other interest	100,000	70,000	10,000(1)			180,000		180,000
Gross rents			60,000			60,000		60,000
Gross royalties						0		0
Net gains and losses	(100,000)	140,000			80,000	120,000	(140,000)	(20,000)
Other income (partnership loss)	(30,000)		(150,000)			(180,000)		(180,000)
Total Income	$1,420,000	$1,710,000	$820,000	$1,100,000	$1,080,000	$6,130,000	($150,000)	$5,980,000
Compensation of officers	300,000					300,000		300,000
Salaries & wages	430,000	1,000,000	350,000	570,000	600,000	2,950,000		2,950,000
Repairs						0		0
Bad debts						0		0
Rents	4,800	30,000	8,000	7,200		50,000		50,000
Taxes	99,000	20,000	5,000	26,000	22,000	172,000		172,000
Interest	250,000	10,000(1)				260,000		260,000
Contributions						0		0
Depreciation	150,000	50,000	37,000	63,000	23,000	323,000		323,000
Depletion						0		0
Advertising						0		0
Pension, profit-sharing, etc., plans	25,000					25,000		25,000
Employee benefit plans	75,000					75,000		75,000
Other deductions						0		0
Total Deductions	$1,333,800	$1,110,000	$400,000	$666,200	$645,000	$4,155,000		$4,155,000
NET INCOME BEFORE STATE ADJUSTMENTS	$86,200	$600,000	$420,000	$433,800	$435,000	$1,975,000	($150,000)	$1,825,000

(1) Corporation B: $10,000 intercompany interest expense
Corporation C: $10,000 intercompany interest income

SCHEDULE 1 – COMBINED INCOME SUBJECT TO APPORTIONMENT

1-B: STATE ADJUSTMENTS, NONBUSINESS INCOME, AND BUSINESS INCOME SUBJECT TO APPORTIONMENT

	CORP A	CORP B	CORP C	CORP D	CORP E	TOTAL BEFORE ADJUSTMENT	DEFERRED INCOME and RESTORATION ADJUSTMENTS	COMBINED
NET INCOME BEFORE STATE ADJUSTMENTS	$86,200	$600,000	$420,000	$433,800	$435,000	$1,975,000	($150,000)	$1,825,000
ADD:								
Taxes measured by income	5,000	1,000	4,000		2,000	12,000		12,000
California corporation tax	12,000		1,000	23,000	19,000	55,000		55,000
Interest on government obligations						0		0
Capital gain/loss adjustments	10,000					10,000		10,000
Excess depreciation	5,000	3,000	6,000	5,000	(1,000)	18,000		18,000
Excess amortization						0		0
Other additions						0		0
Total Additions	$32,000	$4,000	$11,000	$28,000	$20,000	$95,000		$95,000
DEDUCT:								
Intercompany dividends (Sec. 25106)	200,000					200,000		200,000
Capital gain/loss adjustments						0		0
Additional contributions						0		0
Net interest deduction (enterprise zones)						0		0
Other deductions						0		0
Total Deductions	$200,000	0	0	0	0	$200,000		$200,000
NET INCOME AFTER STATE ADJUSTMENTS	(81,800)	604,000	431,000	461,800	455,000	1,870,000	(150,000)	1,720,000
REVERSE NONBUSINESS ITEMS								
Show as: (INCOME)/LOSS:								
Dividends not deducted above	(150,000)					(150,000)		(150,000)
Interest						0		0
Net rental (income)/loss						0		0
Royalties						0		0
(Gain)/loss from sale of assets						0		0
REVERSE BUSINESS ITEMS								
Capital (gain) Loss (Combined Reporting Groups)					(80,000)	(80,000)		(80,000)
Section 1231 (gain) loss (sale of obsolete equipment)	100,000					100,000		100,000
REVERSE BUSINESS ITEMS SUBJECT TO A SEPARATE APPORTIONMENT FORMULA								
Partnership (income)/loss	30,000		150,000			180,000		180,000
	($101,800)	$604,000	$581,000	$461,800	$375,000	$1,920,000	($150,000)	$1,770,000
Interest Offset from Schedule 4								80,000
UNITARY BUSINESS INCOME SUBJECT TO APPORTIONMENT								**$1,850,000**

SCHEDULE 1 – COMBINED INCOME SUBJECT TO APPORTIONMENT

1-C: INTERCOMPANY TRANSACTIONS

	CORP A	CORP B	CORP C	CORP D	CORP E	COMBINED
Gross Profit						
Restorations						
From 2006	$20,000					$20,000
From 2007	$150,000					$150,000
Deferrals						
From 2007	($180,000)					($180,000)
Net (enter the amount on deferred profit line, Schedule 1-A)	($10,000)					($10,000)
Net Gains and Losses						
Restorations						
Deferrals						
From 2007		($140,000)				($140,000)
Net (enter the amount on net gains and losses line, Schedule 1-A)		($140,000)				($140,000)
Other Income						
Restorations						
Deferrals						
Net (enter the amount on other income line, Schedule 1-A)						
Net restored/deferred income	($10,000)	($140,000)				($150,000)

SCHEDULE 2 – CORPORATION C'S INCOME BEFORE AND AFTER JOINING THE COMBINED REPORTING GROUP

	1/1/07-6/30/07	7/1/07-12/31/07
Net sales	$1,210,000	$1,900,000
Cost of goods sold	(900,000)	(1,000,000)
Gross profit	310,000	900,000
Other interest	8,000	10,000
Gross rents	60,000	60,000
Other income (partnership loss)	0	(150,000)
Total Income	$378,000	$820,000
Salaries & wages	307,000	350,000
Rents	7,000	8,000
Taxes	3,000	5,000
Depreciation	32,000	37,000
Net Income Before State Adjustments	29,000	420,000
Taxes Measured by Income	800	4,000
California Corporation Tax	200	1,000
Excess depreciation	5,000	6,000
Net Income After State Adjustments	35,000	431,000
Separate apportionment %	71.4286%	
Nonbusiness Items		
Partnership (income)/loss	0	150,000
Unitary business income (to Schedule 1-A)	0	581,000
Separate CA Income (not in combined report)		
(To Schedule 5-F)	25,000	0
Separate CA AMTI (AMTI adjustments not shown)		
(To Schedule 6-C)	30,000	0

SCHEDULE 3 – COMPUTATIONS TO PLACE CORPORATION D'S INCOME AND APPORTIONMENT FACTORS ON A CALENDAR YEAR BASIS

Year Ended:	**9/30/07 ACTUAL**	**9/12 of 9/30/07**	**9/30/08 ACTUAL**	**3/12 of 9/30/08**	**TOTAL 12/31/07**
Net sales	$2,800,000	$2,100,000	$2,000,000	$500,000	$2,600,000
Cost of goods sold	($1,600,000)	($1,200,000)	($1,200,000)	($300,000)	($1,500,000)
Gross Profit	$1,200,000	$900,000	$800,000	$200,000	$1,100,000
Salaries & wages	$600,000	$450,000	$480,000	$120,000	$570,000
Rents	$7,200	$5,400	$7,200	$1,800	$7,200
Taxes	$28,000	$21,000	$20,000	$5,000	$26,000
Depreciation	$60,000	$45,000	$72,000	$18,000	$63,000
California corporation tax	$24,000	$18,000	$20,000	$5,000	$23,000
Excess depreciation	$4,000	$3,000	$8,000	$2,000	$5,000
Nonbusiness income items	0	0	0	0	0
Property everywhere (year end)					
Inventory	$128,000	$96,000	$176,000	$44,000	$140,000
Fixed depreciable assets	$420,000	$315,000	$460,000	$115,000	$430,000
Land	$10,000	$7,500	$10,000	$2,500	$10,000
California property (year end)					
Inventory	$12,000	$9,000	$20,000	$5,000	$14,000
Fixed depreciable assets	$24,000	$18,000	$28,000	$7,000	$25,000
Rent expense	$1,800	$1,350	$1,800	$450	$1,800
Payroll everywhere	$696,000	$522,000	$540,000	$135,000	$657,000
California payroll	$16,000	$12,000	$100,000	$25,000	$37,000
Sales everywhere	$2,800,000	$2,100,000	$2,000,000	$500,000	$2,600,000
California sales	$716,000	$537,000	$1,000,000	$250,000	$787,000

Note: The Total column is the sum of the 9/12 column and the 3/12 column.

SCHEDULE 4 – CALCULATION OF COMBINED INTEREST OFFSET

		COMBINED TOTALS	
1	Total interest expense deducted	$260,000	
2	Water’s-edge offset (from form FTB 2424)	0	
3	Net interest expense (amount on line 1 less amount on line 2)		$260,000
4	Total interest income	$180,000	
5	Less nonbusiness interest income	0	
6	Business interest income		$180,000
7	Balance: line 3 minus line 6, but not less than zero		$80,000
8	Total dividend income	$350,000	
9a	Less water’s-edge dividends deducted	0	
b	Less intercompany dividends deducted	($200,000)	
10	Balance	$150,000	
11	Business dividend income	0	
12	Net nonbusiness dividend income (line 10 minus line 11)		$150,000
13	Total nonbusiness interest and dividends (line 5 plus line 12)		$150,000
14	Interest offset (assignable 100% to Corp A) (enter lesser of line 7 or line 13)		$80,000

In the example only one entity has California nonbusiness dividend income. If more than one entity had California nonbusiness interest and/or nonbusiness dividend income, the interest offset would be prorated between entities by the ratio of each entity’s California nonbusiness interest and/or nonbusiness dividends to the total California nonbusiness interest and nonbusiness dividends. For more information, see FTB Notice 2000-9 regarding the policy for the application of R&TC Section 24344(b).

Note: A contributions adjustment applicable to nonbusiness income of multiple entities may also require such computations.

SCHEDULE 5 – COMBINED APPORTIONMENT FORMULA AND ENTITY INCOME ASSIGNMENT

5-A: COMBINED APPORTIONMENT DATA

PROPERTY FACTOR	CORP A	CORP B	CORP C	CORP D (pro-rated from Sch. 3)	CORP E	COMBINED
Property everywhere						
Inventory – 12/31/07	100,000	150,000		140,000	120,000	
Fixed depreciable assets – 12/31/07	1,100,000	310,000	See Monthly	430,000	430,000	
Land – 12/31/07	50,000	0	Average	10,000	100,000	
Less intercompany profit included above	0	0	Computation	(140,000)[1]	(30,000)	
Total – end of year	1,250,000	460,000	(Sch. 5-B)	440,000	620,000	
Total – beginning of year (from 2006 report)	1,370,000	575,000		755,000	580,000	
Total beginning and ending	2,620,000	1,035,000		1,195,000	1,200,000	
Average owned property (divide by 2)	1,310,000	517,500	175,000	597,500	600,000	3,200,000
Rent expense (excluding intercompany and nonbusiness)	4,800	30,000	8,000	7,200	0	50,000
Capitalize (multiply by 8)	38,400	240,000	64,000	57,600		400,000
Combined property everywhere	1,348,400	757,500	239,000	655,100	600,000	3,600,000
California property						
Inventory – 12/31/07	41,000	0		14,000	95,000	
Fixed depreciable assets – 12/31/07	400,000	0	See Monthly	25,000	330,000	
Land – 12/31/07	20,000	0	Average	0	70,000	
Less intercompany profit included above	0	0	Computation	0	0	
Total – end of year	461,000	0	(Sch. 5-B)	39,000	495,000	
Total – beginning of year (from 2006 report)	427,000	0		47,000	453,000	
Total beginning and ending	888,000	0		86,000	948,000	
Average owned property (divide by 2)	444,000	0	175,000	43,000	474,000	1,136,000
Rent expense (excluding intercompany and nonbusiness)	1,200	0	8,000	1,800	0	11,000
Capitalize (multiply by 8)	9,600	0	64,000	14,400	0	88,000
Combined California property	453,600	0	239,000	57,400	474,000	1,224,000

1 – The $140,000 is removed to return the fixed asset purchased from Corporation B to its original cost basis of $70,000.

SCHEDULE 5 – COMBINED APPORTIONMENT FORMULA AND ENTITY INCOME ASSIGNMENT

5-B: COMPUTATION OF AVERAGE PROPERTY VALUES FOR CORP C (PARTIAL YEAR COMBINATION)

MONTHLY AMOUNTS TO BE INCLUDED IN THE COMBINED PROPERTY FACTOR

	INVENTORY	FIXED DEPRECIABLE	LAND	TOTAL
January	0	0	0	0
February	0	0	0	0
March	0	0	0	0
April	0	0	0	0
May	0	0	0	0
June	0	0	0	0
July	$10,000	$260,000	$30,000	$300,000
August	50,000	260,000	30,000	340,000
September	60,000	260,000	30,000	350,000
October	70,000	260,000	30,000	360,000
November	80,000	260,000	30,000	370,000
December	90,000	260,000	30,000	380,000
TOTAL	$360,000	$1,560,000	$180,000	$2,100,000
AVERAGE	$30,000	$130,000	$15,000	$175,000

Note: All of Corporation C's owned tangible property is located in California, so the same amounts will be included in both the numerator and denominator of the property factor (see Schedule 5-A).

SCHEDULE 5 – COMBINED APPORTIONMENT FORMULA AND ENTITY INCOME ASSIGNMENT

5-C: COMBINED APPORTIONMENT DATA

PAYROLL FACTOR	CORP A	CORP B	CORP C	CORP D	CORP E	COMBINED
Payroll everywhere	1,630,000	1,293,000	420,000	657,000	750,000	4,750,000
California payroll	553,000	0	210,000	37,000	530,000	1,330,000
SALES FACTOR						
Sales everywhere						
Gross receipts, less returns and allowances	7,000,000	4,000,000	1,900,000	2,600,000	2,600,000	18,100,000
Other gross receipts (rents, royalties, etc.)	270,000[1]	280,000[2]	70,000[3]	0	0	620,000
Sale of stock					400,000[6]	400,000
Less intercompany receipts	(600,000)	(210,000)	(10,000)[4]	0	0	(820,000)
Total sales everywhere	6,670,000	4,070,000	1,960,000	2,600,000	3,000,000	18,300,000
California sales						
Sales delivered or shipped to California purchasers:						
i) Shipped from outside California		0[5]				0
ii) Shipped from within California	3,000,000		1,190,000	787,000	1,292,000	6,269,000
Sales shipped from California by a unitary member to:						
i) The United States Government						0
ii) Purchasers in a state where the corporations immune under Public Law 86-272	100,000					100,000
Other gross receipts (rents, royalties, etc.)	128,000		70,000[3]			198,000
Less intercompany receipts	(400,000)		(10,000)[4]			(410,000)
Total California sales	2,828,000	0	1,250,000	787,000	1,292,000	6,157,000

(1) Equipment sale = $170,000
Interest = 100,000
(2) Equipment sale = $210,000
Interest = 70,000
(3) Interest = $10,000
Rents = 60,000
(4) Intercompany interest income
(5) Sales not assigned to California because Corporation B does not have Nexus
(6) Sale of business capital assets

SCHEDULE 5 – COMBINED APPORTIONMENT FORMULA AND ENTITY INCOME ASSIGNMENT

5-D: COMBINED APPORTIONMENT FACTORS AND ENTITY INCOME ASSIGNMENT

Line			CORP A	CORP B	CORP C	CORP D	CORP E	COMBINED
1	EVERYWHERE:	Property						3,600,000
2		Payroll						4,750,000
3		Sales						18,300,000
4	CALIFORNIA:	Property	453,600	0	239,000	57,400	474,000	1,224,000
5		Payroll	553,000	0	210,000	37,000	530,000	1,330,000
6		Sales	2,828,000	0	1,250,000	787,000	1,292,000	6,157,000
7	UNITARY BUSINESS INCOME TO BE APPORTIONED (from Schedule 1-B)							1,850,000
	CALIFORNIA APPORTIONMENT PERCENT (California property, payroll, sales divided by combined property, payroll, sales)							
8	Property factor (line 4 ÷ line 1)		12.6000%		6.6389%	1.5944%	13.1667%	34.0000%
9	Payroll factor (line 5 ÷ line 2)		11.6421%		4.4211%	0.7789%	11.1579%	28.0000%
10	Sales factor (line 6 ÷ line 3) x 2		30.9072%		13.5870%	8.5543%	14,0435%	67.0920%
11	Total		55.1493%		24.6469%	10.9277%	38.3680%	129.0920%
12	Apportionment percentage (divide by 4)		13.7873%	0.0000%	6.1617%	2.7319%	9.5920%	32.2729%
13	BUSINESS INCOME ASSIGNED TO CALIFORNIA (Line 7 x line 12)		$255,065	0	$113,991	$50,540	$177,452	$597,049

SCHEDULE 5 - COMBINED APPORTIONMENT FORMULA AND ENTITY INCOME ASSIGNMENT
5-E: CAPITAL GAIN (LOSS)

	CORP A	CORP B	CORP C	CORP D	CORP E	COMBINED
Period for which California return is to be filed	1/1/07-12/31/07	None	7/1/07-12/31/07	10/1/06-9/30/07	1/1/07-12/31/07	
Apportionment percentage (from Sch. 5D)	13.7873%	0.0000%	6.1617%	2.7319%	9.5920%	32.2729%
Section 1231: $100,000 loss from Corporation A (sale of obsolete equipment)	(13,787)		(6,162)	**2,049	(9,592)	(31,590)
Business capital stock gain apportioned to California ($100,000 from Corporation E)	13,787	0	6,162	*2,049	9,592	31,590
Nonbusiness capital stock loss (from Corporation E)					(20,000)	
Post-apportioned capital gains (losses) netting	0	0	0	0	*** (20,000)	0

* Corporation D's apportionment shares of the business capital gain is adjusted to reflect the defiscalization. ($100,000 x 2.7319% = $2,732 x 9/12's = $2,049)

** Corporation D's apportionment share of Section 1231 loss is adjusted to reflect the defiscalization ($100,000 x 2.7319% = $2,732 x 9/12's = $2,049).

*** Corporation E has a California sourced carryover loss of $10,408.

SCHEDULE 5 – COMBINED APPORTIONMENT FORMULA AND ENTITY INCOME ASSIGNMENT

5-F: CALIFORNIA NET INCOME AND TAX

	CORP A	CORP B	CORP C	CORP D	CORP E
Period for which California return is to be filed	1/1/07-12/31/07	None	7/1/07-12/31/07	10/1/06-9/30/07	1/1/07-12/31/07
BUSINESS INCOME APPORTIONED TO CALIFORNIA					
CORP A (from Schedule 5-D)	$255,065				
CORP C (from Schedule 5-D)			$113,991		
CORP D:					
For 12 months ended 12/0 (from Schedule 5-D)				$50,540	
Portion reportable in current year (9/12)				$37,905	
For 12 months ended 12/06 prior year calculation				$50,000	
Portion reportable in current year (3/12)				$12,500	
CORP D total for year ended 9/30/07				$50,405	
CORP E: (from Schedule 5-D)					$177,452
Nonbusiness income (losses) wholly					
attributable to California					
Dividends	$150,000				
Net rental income/(loss)					
Gain/(loss) on sale of assets					
Business income (loss) subject to a separate apportionment formula					
Partnership income (loss)	($30,000)		($150,000)		
Total	$375,065	0	($36,009)	$50,405	$177,452
Interest offset (from Schedule 4)	($80,000)				
Post apportioned and allocated amounts from capital gain/loss					
netting combined reporting groups (Schedule 5-E)	0	0	0	0	0
Net income before contributions adjustment	$295,065	0	($36,009)	$50,405	$177,452
Contributions adjustment					
Add California separate net income for pre-acquisition period					
1/1/07 - 6/30/07 (Schedule 2 cannot be included in the combined report)			$25,000		
Net income (loss) for state purposes	$245,065	0	($11,009)	$50,405	$177,452
Net Operating Losses (NOL) Deduction					
NOL carryover deduction	($25,000)				
EZ, LARZ, or LAMBRA NOL carryover deduction	($50,000)				
Disaster Loss carryover deduction					($100,000)
Net income for tax purposes	$220,065		($11,009)	$50,405	$77,452
Franchise Tax (8.84% tax rate), or $800 minimum tax, if applicable	$19,454	0	$800	$4,456	$6,847
Credits					
Credit Name Salmon/Trout code no. 200 (carryover)				($500)	
Credit Name Research code no. 183					($2,000)
Credit Name Disabled Access code no 205				($125)	
Alternative Minimum Tax (from Schedule 6-C)	$3,808	0	$11,595	0	$3,024
TOTAL TAX	$23,262	0	$12,395	$3,831	$7,871

SCHEDULE 6 – COMBINED ALTERNATIVE MINIMUM TAX

6-A: ALTERNATIVE MINIMUM TAXABLE INCOME

		CORP A	CORP B	CORP C	CORP D	CORP E	TOTAL BEFORE ADJUSTMENT	DEFERRED INCOME and RESTORATION ADJUSTMENTS	COMBINED
1	**NET INCOME AFTER STATE ADJUSTMENTS (From Schedule 1-B)**	($81,800)	$604,000	$431,000	$461,800	$455,000	$1,870,000	($150,000)	$1,720,000
	AMT ADJUSTMENTS & PREFERENCES:								
2a	Depreciation	40,000	4,000	3,000	6,000	(1,000)	52,000		52,000
2b	Basis adjustment in determining gain or loss from sale/exchange	2,000					2,000		2,000
2c	Depletion	40,000(1)		200,000(2)			240,000		240,000
2d	Intangible drilling costs	10,000 (1)		15,000(2)			25,000		25,000
3	**TOTAL AMTI**	($10,200)	$608,000	$649,000	$467,800	$454,000	$2,189,000	($150,000)	$2,039,000
	LESS NONBUSINESS ITEMS (adjusted for AMTI)						0		0
4a	Dividends	(150,000)					(150,000)		(150,000)
4b	Partnership (income)/loss subject to a separate apportionment formula	(20,000)(3)		(65,000)(4)			(85,000)		(85,000)
	Add: Interest offset	80,000					80,000		80,000
5	Unitary business AMTI	(79,800)	608,000	584,000	467,800	454,000	2,034,000	(150,000)	1,884,000
6	Apportionment percentage (from Schedule 5-D, line 12)	13.7873%	0.0000%	6.1617%	2.7319%	9.5920%			32.2729%
7	Combined business AMTI apportioned to California (line 5 x line 6)	259,753	0	116,086	51,469	180,713			608,021
	Nonbusiness items allocated to California (adjusted for AMTI)								
8	Dividends	150,000							
9	Partnership income/(loss) subject to a separate apportionment formula	20,000(3)		65,000(4)					
	Less: Interest offset	(80,000)							
10	PRE-ADJUSTMENT AMTI	349,753	0	181,086	51,469	180,713			
11	ACE adjustment (from Schedule 6-B)	52	0	23	10	36			
12	**ALTERNATIVE MINIMUM TAXABLE INCOME**	$349,805	0	$181,109	$51,479	$180,749			

(1) From nonunitary partnership
(2) From nonunitary partnership
(3) ($30,000) – $50,000 AMTI items = $20,000 adjusted partnership AMTI
(4) ($150,000) – $215,000 AMTI items = $65,000 adjusted partnership AMTI

SCHEDULE 6 – COMBINED ALTERNATIVE MINIMUM TAX

6-B: ACE ADJUSTMENT

		CORP A	CORP B	CORP C	CORP D	CORP E	TOTAL BEFORE ADJUSTMENT	DEFERRED INCOME and RESTORATION ADJUSTMENT	COMBINED
1	**TOTAL AMTI (from Schedule 6-A, line 3)**	($10,200)	$608,000	$649,000	$467,800	$454,000	$2,189,000	($150,000)	$2,039,000
	ADJUSTMENT FOR ACE:								
2	Basis adjustment in determining gain or loss from sale/exchange	500					500		500
3	Pre-apportioned ACE	(10,700)	608,000	649,000	467,800	454,000	2,189,500	(150,000)	2,039,500
	LESS NONBUSINESS ITEMS (adjusted for ACE):								
4a	Dividends	(150,000)					(150,000)		(150,000)
4b	Partnership income (loss) subject to a separate apportionment formula	(20,000)		(65,000)			(85,000)		(85,000)
	Add: Interest offset	80,000					80,000		80,00
5	Pre-apportionment business ACE						2,034,500	(150,000)	1,884,500
6	Apportionment percentage (from Schedule 5-D, line 12)	13.7873%	0.0000%	6.1617%	2.7319%	9.5920%			32.2729%
7	Business ACE apportioned to California	259,822	0	116,117	51,483	180,761			608,183
	Nonbusiness items allocated to California (adjusted for ACE)								
8	Dividends	150,000							
9	Partnership income (loss) subject to a separate apportionment formula	20,000		65,000					
	Less: Interest offset	(80,000)							
10	ADJUSTED CURRENT EARNINGS	349,822	0	181,117	51,483	180,761			
11	Pre-adjustment AMTI (Schedule 6-A, line 10)	349,753	0	181,086	51,469	180,713			
12	Difference	69	0	31	14	48			
13	75% of Difference	52	0	23	10	36			
14	Negative ACE limitation: for each taxpayer excess of aggregate prior year positive line 13 ACE adjustments over aggregate prior year negative line 13 ACE adjustments:	0	0	0	0	0			
15	**ACE ADJUSTMENT***	$52	0	$23	$10	$36			

* If line 13 is negative, it is allowed as a negative ACE adjustment only to the extent of that taxpayer's total increases in AMTI from prior year California ACE adjustments exceed its total reduction in AMTI from prior year California ACE adjustments.

SCHEDULE 6 – COMBINED ALTERNATIVE MINIMUM TAX

6-C: ALTERNATIVE MINIMUM TAX

	CORP A	CORP B	CORP C	CORP D	CORP E
Period for which California return is to be filed	1/1/07-12/31/07	None	7/1/07-12/31/07	10/1/06-9/30/07	1/1/07-12/31/07
CALIFORNIA AMTI (from Schedule 6-A)					
CORP A	$349,805				
CORP C			$181,109		
Add California separate AMTI for					
pre-acquisition period 1/1/07-6/30/07 (Schedule 2)			$30,000		
CORP D:					
For 12 months ended 12/07				$51,479	
Portion reportable in current year (9/12)				$38,609	
For 12 months ended 12/06 (from prior year calculation)				$53,000	
Portion reportable in current year (3/12)				$13,250	
CORP D Total				$51,859	
CORP E					$180,749
AMTI ADJUSTED FOR EACH CORPORATION'S TAXABLE YEAR	$349,805	0	$211,109	$51,859	$180,749
Less exemption (subject to phaseout when AMTI exceeds $150,000)	0		($24,723)	($40,000)	($32,313)
AMTI subject to tax	$349,805	0	$186,386	$11,859	$148,436
Tentative minimum tax (6.65% tax rate)	$23,262	0	$12,395	$789	$9,871
Less regular franchise or income tax (from Schedule 5-F)	$19,454	0	$800	$4,456	$6,847
ALTERNATIVE MINIMUM TAX	$3,808	0	$11,595	0	$3,024

How To Get California Tax Information

Where To Get Tax Forms and Publications

By Internet – You can download, view, and print California tax forms, instructions, publications, FTB Notices, and Legal Rulings from our Website at **www.ftb.ca.gov**.

By phone – You can order current year California tax forms between 6 a.m. and 8 p.m. Monday through Friday, except holidays.

- Refer to the list in the right column and find the code number for the form you want to order.
- Call (800) 338-0505.
- Select "Business Entity Information."
- Select "Forms and Publications."
- Enter the three-digit code shown to the left of the form title when instructed.

Allow two weeks to receive your order. If you live outside California, allow three weeks to receive your order.

In person – Many libraries have forms and schedules for you to photocopy (a nominal fee may apply).

Employees at libraries cannot provide tax information or assistance.

By mail – Write to:

TAX FORMS REQUEST UNIT
FRANCHISE TAX BOARD
PO BOX 307
RANCHO CORDOVA CA 95741-0307

Letters

If you write to us, be sure to include your California corporation number or federal employer identification number, your daytime and evening telephone numbers, and a copy of the notice with your letter. Send your letter to:

FRANCHISE TAX BOARD
PO BOX 942857
SACRAMENTO CA 94257-0540

We will respond to your letter within ten weeks. In some cases, we may need to call you for additional information. Do not attach correspondence to your tax return unless the correspondence relates to an item on the return.

General Toll-Free Phone Service

Telephone assistance is available year-round from 7 a.m. until 6 p.m. Monday through Friday, except holidays.

From within the United States . . . . (800) 852-5711
From outside the United States (not toll-free) . . . . (916) 845-6500
For federal tax questions, call the IRS at . . . . (800) 829-1040

Assistance for persons with disabilities
We comply with the Americans with Disabilities Act. Persons with hearing or speech impairment, please call:

TTY/TDD . . . . (800) 822-6268

Asistencia bilingüe en español:
Asistencia telefónica esta disponible todo el año durante las 7 a.m. y las 6 p.m. lunes a viernes, excepto días festivos.
Dentro de los Estados Unidos, llame al . . . . (800) 852-5711
Fuera de los Estados Unidos, llame al
(cargos aplican) . . . . (916) 845-6500
Para preguntas sobre impuestos federales,
llame el IRS al . . . . (800) 829-1040

California Tax Forms and Publications

817 California Corporation Tax Forms and Instructions.
This booklet contains:
Form 100, California Corporation Franchise or Income Tax Return;
Schedule H (100), Dividend Income Deductions
Schedule P (100), Alternative Minimum Tax and Credit Limitations — Corporations
FTB 3539, Payment for Automatic Extension for Corps and Exempt Orgs
FTB 3565, Small Business Stock Questionnaire
FTB 3805Q, Net Operating Loss (NOL) Computation and NOL and Disaster Loss Limitations — Corporations
FTB 3885, Corporation Depreciation and Amortization

816 California S Corporation Tax Forms and Instructions.
This booklet contains:
Form 100S, California S Corporation Franchise or Income Tax Return;
Schedule B (100S), S Corporation Depreciation and Amortization
Schedule C (100S), S Corporation Tax Credits
Schedule D (100S), S Corporation Capital Gains and Losses and Built-In Gains
Schedule H (100S), Dividend Income Deduction
Schedule K-1 (100S), Shareholder's Share of Income, Deductions, Credits, etc.
Schedule QS, Qualified Subchapter S Subsidiary (QSub) Information Worksheet
FTB 3539, Payment for Automatic Extension for Corps and Exempt Orgs
FTB 3805Q, Net Operating Loss (NOL) Computation and NOL Disaster Loss – Corporations

814 Form 109 Booklet, California Exempt Organization Business Income Tax Return
818 Form 100-ES, Corporation Estimated Tax
815 Form 199, California Exempt Organization Annual Information Return and Instructions
802 FTB 3500, Exemption Application

Your Rights As A Taxpayer

Our goal at the FTB is to make certain that your rights are protected so that you will have the highest confidence in the integrity, efficiency, and fairness of our state tax system. FTB Pub. 4058, California Taxpayers' Bill of Rights, includes information on your rights as a California taxpayer, the Taxpayers' Rights Advocate Program, and how you can request written advice from the FTB on whether a particular transaction is taxable.

See "Where to Get Tax Forms and Publications" on this page.

Automated Toll-Free Phone Service (Keep This Booklet For Future Use)

Use our automated toll-free phone service to get recorded answers to many of your questions about California taxes and to order current year California business entity tax forms and publications. This service is available in English and Spanish to callers with touch-tone telephones. Have paper and pencil ready to take notes.

Call from within the United States	(800) 338-0505
Call from outside the United States (not toll-free)	(916) 845-6600

To Order Forms

See "Where to Get Tax Forms and Publications" on the previous page.

To Get Information

You can hear recorded answers to Frequently Asked Questions 24 hours a day, 7 days a week. Call our automated phone service at the number listed above. Select "Business Entity Information," then select "Frequently Asked Questions." Enter the 3-digit code, listed below, when prompted.

Code Filing Assistance

715 If my actual tax is less than the minimum franchise tax, what figure do I put on line 24 of Form 100 or Form 100W?
717 What are the tax rates for corporations?
718 How do I get an extension of time to file?
722 When does my corporation have to file a short-period return?
734 Is my corporation subject to franchise tax or income tax?

S Corporations

704 Is an S corporation subject to the minimum franchise tax?
705 Are S corporations required to make estimated payments?
706 What forms do S corporations file?
707 The tax for my S corporation is less than the minimum franchise tax. What figure do I put on line 22 of Form 100S?

Exempt Organizations

709 How do I get tax-exempt status?
710 Does an exempt organization have to file Form 199?
736 I have exempt status. Do I need to file Form 100 or Form 109 in addition to Form 199?

Minimum Tax and Estimate Tax

712 What is the minimum franchise tax?
714 My corporation is not doing business; does it have to pay the minimum franchise tax?

Billings and Miscellaneous Notices

503 How do I file a protest against a Notice of Proposed Assessment?
723 I received a bill for $250. What is this for?

Corporate Dissolution

724 How do I dissolve my corporation?

Limited Liability Companies (LLC)

750 How do I organize or register an LLC?
752 What tax forms do I use to file as an LLC?
753 When is the annual tax payment due?

Miscellaneous

700 Who do I need to contact to start a business?
701 I need a state Employer ID number for my business. Who do I contact?
703 How do I incorporate?
737 Where do I send my payment?